



United States Department of the Interior



BUREAU OF LAND MANAGEMENT

Montana State Office

5001 Southgate Drive, P.O. Box 36800

Billings, Montana 59107-6800

<http://www.mt.blm.gov/>

IN REPLY TO:

SDR-922-01-09

3160 (922.WL)

June 22, 2001

CERTIFIED-RETURN RECEIPT REQUESTED

DECISION

Mr. John W. Morrison)
Fleck, Mather & Strutz, LTD)
P.O. Box 2798)
Bismark, North Dakota 58502)

SDR No. 922-01-09

AFFIRMED

Whiting Petroleum Corporation (Whiting) requests a State Director Review (SDR) in accordance with 43 CFR 3165.3(b) of the May 16, 2001, decision of the North Dakota Field Office (NDFO) Assistant Field Manager denying an alternative royalty sharing arrangement for a Communitization Agreement (CA) covering the W $\frac{1}{4}$ of Section 8, T. 138 N., R. 100 W. The SDR request was considered timely filed on June 7 and was assigned number SDR 922-01-09.

BACKGROUND

On May 11, 2001, Whiting submitted a request to the NDFO requesting approval of a royalty sharing arrangement for Madison Fryburg production from the W $\frac{1}{4}$ of Section 8, T. 138 N., R. 100 W. The royalties would be shared on such a basis so as to allow 65 percent of the production to be allocated to the NW $\frac{1}{4}$ and 35 percent to the SW $\frac{1}{4}$. The oil and gas underlying the SW $\frac{1}{4}$ is owned by the United States of America and is leased to Whiting, et al. The oil and gas underlying the NW $\frac{1}{4}$ is owned by the State of North Dakota and is leased to Upton Resources USA.

A vertical well (the Federal No. 8-14) was drilled and completed in the Madison Formation in the SW $\frac{1}{4}$ SW $\frac{1}{4}$ of Section 8 in 1988. Through April 2001, the well has produced 66,587 barrels of oil. Spacing for vertical wells in this section is one well per 160 acres. Therefore, all royalties attributed to this well have been paid to the United States. Whiting and other companies in the area have recently undertaken horizontal drilling activities in the immediate vicinity of this lease. Typical spacing for horizontal wells in the area is one well per 320 acres or 2 wells per 640 acres. The E $\frac{1}{4}$ of Section 8 is spaced at one well per 320 acres. Whiting is proposing to drill a horizontal well in the W $\frac{1}{4}$ of Section 8. Since 66,758 barrels of oil have already been produced from the SW $\frac{1}{4}$ from the vertical well, Whiting does not

believe it would be fair to share royalties from a horizontal well on a 50/50 percent basis based on acreage.

Whiting's 65/35 percent proposal is based on calculations that show there are 320,000 barrels of recoverable oil per 320 acre spacing unit in this area. Based on these recoverable reserves, the NW $\frac{1}{4}$ would contain 160,000 barrels and the SW $\frac{1}{4}$ would contain 160,000 barrels. However, approximately 70,000 barrels of oil have already been produced from the SW $\frac{1}{4}$. Therefore, only 250,000 barrels of recoverable reserves remain in the spacing unit with the NW $\frac{1}{4}$ contributing 160,000 barrels and the SW $\frac{1}{4}$ contributing 90,000 barrels. This results in the 65/35 percent proportionate split.

Whiting states in their request that:

"There is no geologic or engineering data that would support the original recoverable reserves in each of the 160 acre blocks composing the W/2 of Section 8 were not equal. All evidence to date suggests that the two blocks are similar in their geologic makeup."

On May 16, the NDFO Assistant Field Manager sent a letter to Whiting denying the request. The NDFO based their decision on guidance contained in BLM Manual 3160-9 - Communitization (Manual). The letter states that because there are no provisions for approving a CA allocating production on any basis other than surface acreage, the request cannot be approved.

ARGUMENTS

Whiting argues that:

"The Field Office erred in failing to even consider whether the proposed royalty sharing arrangement in the context of a CA was in the public interest of the United States and, instead, relied solely upon a mechanistic reading of the BLM Manual. Although the Field Office notes that the policy set forth in the Manual allows for deviation from the model form, the Field Office asserts that the Manual requires the allocation of production under any CA to be based solely upon surface acreage."

Whiting also argues that, "nothing in the Manual explicitly states that any tract allocation must be based **solely** upon the surface acreage contained in the various tracts."

Whiting argues that while allocation may ordinarily be best accomplished on a surface acreage basis, this is not an ordinary case. Whiting cites an e-mail transmission, dated May 2, from a Petroleum Engineer of the NDFO in which he stated:

"In reality this [proposal to split royalties on a 65/35 basis] does seem reasonable, since we did already 'at least partially drain the Madison zone in the SW $\frac{1}{4}$.'"

Whiting also references an e-mail transmission dated May 4, from a Supervisory Petroleum Engineer of the Montana State Office in which he indicated that while such an allocation would be unusual, it could be accomplished and that,

if such an allocation was approved by the North Dakota Industrial Commission, the CA would need to refer to the NDIC order. He further noted that on at least one occasion, the NDFO had approved a CA in which production was allocated on the basis of the percentage of a horizontal leg within a unit.

DISCUSSION

Guidance for processing applications for communitized area is contained in BLM Manual 3160-9 - Communitization. Appendix 1 of this Manual provides the model CA form. While deviation from the model form can be approved, the model form was developed to provide fair and consistent handling of communitization applications. The Manual is clear as to the information to be included if a deviation from the model form is requested. The Manual states:

If deviations from the form are justified, the revised or changed form shall:

1. Describe the separate tracts comprising the drilling or spacing unit.
2. Show the tract allocation, based on surface acreage, of communitized substances to the communitized tracts (emphasis added).

The NDFO was correct in their interpretation of the Manual in that there are no provisions for approving a CA allocating production on any basis other than surface acreage. Allocating production from a communitized area on the basis of surface acreage is a reasonable and equitable method of handling production. It is widely understood and accepted by industry, State agencies, and Federal agencies. It is also understood that oil and gas will not be produced uniformly from every acre included in a CA. This can be due to many factors including differences in the quality of reservoir rock within the CA area, and the fact that reservoir drainage does not conform to governmental surveys.

However, this situation is unique because of the existing vertical well and the change in spacing to accommodate advanced technology. Therefore, consideration should be given to Whiting's proposal.

In this case, Whiting has knowledge of the production from the existing well along with general knowledge of the area. They have determined that a 320 acre spacing unit contains around 320,000 barrels of recoverable reserves. This recoverable reserve, however, is based on data from other wells in the field and assumes a homogeneous reservoir. Whiting has stated:

"There is no geologic or engineering data that would support the original recoverable reserves in each of the 160-acre blocks composing the W $\frac{1}{2}$ of Section 8 were not equal."

This does not necessarily mean that the reserves in each of the 160 acre blocks is equal. Whiting also states that, "All evidence to date suggests that the two blocks are similar in their geologic makeup." However, evidence before the North Dakota Industrial Commission contradicts this statement. Finding 15 in the Commissions Order No. 8919 states, "Evidence indicates the quality of reservoir rock varies significantly across the sections...." Therefore, we cannot be sure that the calculated recoverable reserves are correct nor can we be sure of how the reserves are distributed throughout the spacing unit. If the calculated recoverable reserves are incorrect, the proposed allocation of production would be incorrect.

Our review of the information submitted by Whiting has not shown conclusively that oil will be produced on a 65/35 percent basis. Additional analysis is necessary to make a conclusive determination. This analysis should include considerations such as: 1) the area of drainage from the existing vertical well (i.e., Well No. 8-14 is not located in the center of the SW¼. Some of the 66,587 barrels of oil produced from the well may be coming from an adjacent section), 2) the drainage area of the proposed horizontal well, 3) the length and location of the horizontal section of the well, 4) any geologic anomalies that may affect production, and 5) any other applicable engineering or geologic data. If this type of detailed analysis can conclusively show that a split different from the accepted 50/50 percent split is appropriate, it should be considered.

Whiting references an e-mail transmission from NDFO staff in which it is stated that the proposed 65/35 percent split seems reasonable. While this may have been his initial reaction to the proposal, it was generated prior to reviewing Whiting's written proposal. The BLM's official response to the proposal is contained in the May 16 letter, from the Assistant Field Managers to Whiting.

Whiting also references an e-mail transmission from the State Office Engineer in which he indicated that while such an allocation would be unusual, it could be accomplished. Again, this was preliminary discussion on the proposal and was generated prior to reviewing the written request. The e-mail further noted that on at least one occasion, the NDFO had approved a CA in which production was allocated on the basis of the percentage of a horizontal leg within a unit. Again, this was preliminary discussion on the proposal. Further review revealed that the referenced situation did not involve a CA. It involved two Federal units where spacing is not applicable. Therefore, it is not related to this case.

DECISION

Approval of the proposed alternative royalty sharing agreement for a Communitization Agreement covering the W¼ of Section 8, T. 138 N., R. 100 W. is not in the public interest of the United States. While deviation from the model CA form can be approved, the information submitted by Whiting has not shown conclusively that oil will be produced from the spacing unit on a 65/35 percent basis. Therefore, the May 16, 2001, decision of the NDFO Assistant Field Manager denying the alternative royalty sharing arrangement is affirmed. If, however, a detailed analysis can conclusively show that a split different from the accepted 50/50 percent split is appropriate, Whiting may resubmit their proposal to the NDFO for consideration.

This Decision may be appealed to the Board of Land Appeals, Office of the Secretary, in accordance with the regulations contained in 43 CFR 4.400 and Form 1842-1 (Enclosure 1). If an appeal is taken, a Notice of Appeal must be filed in this office at the aforementioned address within 30 days from receipt of this Decision. A copy of the Notice of Appeal and of any statement of reasons, written arguments, or briefs must also be served on the Office of the Solicitor at the address shown on Form 1842-1. It is also requested that a copy of any statement of reasons, written arguments, or briefs be sent to this office. The appellant has the burden of showing that the Decision appealed from is in error.

If you wish to file a Petition for a Stay of this Decision, pursuant to 43 CFR 4.21, the Petition must accompany your Notice of Appeal. A Petition for a Stay is required to show sufficient justification based on the standards listed below. Copies of the Notice of Appeal and Petition for a Stay **must** also be submitted to each party named in the Decision and to the Interior Board of Land Appeals and to the appropriate Office of the Solicitor (see 43 CFR 4.413) at the same time the original documents are filed with this office. If you request a stay, you have the burden of proof to demonstrate that a stay should be granted.

Standards for Obtaining a Stay

Except as otherwise provided by law or other pertinent regulation, a petition for a stay of a Decision pending appeal shall show sufficient justification based on the following standards:

- (1) The relative harm to the parties if the stay is granted or denied,
- (2) The likelihood of the appellant's success on the merits
- (3) The likelihood of immediate and irreparable harm if the stay is not granted, and
- (4) Whether the public interest favors granting the stay.



Thomas P. Lonnie
Deputy State Director
Division of Mineral Resources

1 Enclosures

1-Form 1842-1 (1 p)

cc:(w/o encls.)

Mark Seale, Whiting Petroleum Corporation
Rick Larson, North Dakota State Land Department
WO(310), LS, Rm. 406
All BLM State Offices
Great Falls Oil and Gas Field Station
Miles City Field Office
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